APPENDIX A

OPINION BELOW

UNITED STATES COURT OF APPEALS
FOR THE FOURTH CIRCUIT

No. 8244.

UNITED STATES OF AMERICA, *Appellee*,

versus

WOODLAND TERRACE, INC., *Appellant*.

APPEAL FROM THE UNITED STATES DISTRICT COURT FOR THE EASTERN DISTRICT OF SOUTH CAROLINA, AT CHARLESTON.

GEORGE BELL TIMMERMAN, DISTRICT JUDGE.

(Argued January 23, 1961. Decided August 5, 1961.)

Before SOPER, HAYNSWORTH, and BOREMAN, Circuit Judges.

Louis M. Shimel and J. C. Long (W. Turner Logan on brief) for Appellant, and George E. Lewis, Assistant United States Attorney, (N. Welch Morrisette, Jr., United States Attorney, on brief) for appellee.

HAYNSWORTH, Circuit Judge:

At issue is the right of the United States to foreclose a mortgage on a rental housing project, a mortgage which it had insured through the Federal Housing Administration and later, after the mortgagor's default, acquired by assignment. The Master, to whom the matter was referred, and the District Court found no impediment in the right of foreclosure. We find none.

Woodland Terrace, Inc. was organized in 1949 in South Carolina for the purpose of constructing and operating a rental housing project under § 608 of the National Housing Act.[1] Its charter was in the form approved by FHA. That agency was the owner of an entire issue of preferred stock, having an aggregate par value of $100. The project's individual sponsors acquired 259 shares of common stock having an aggregate par value of $25,900 in exchange for the land near Columbia, S. C., upon which the improvements were to be erected.

Woodland Terrace obtained from Wachovia Bank and Trust Company a loan, insured by FHA, of $1,256,100 payable interest only through October 1950 and thereafter in monthly instalments of principal and interest of $5,757.12 over a period of approximately thirty-three years. The loan was evidenced by a note and secured by a mortgage on forms approved by FHA.

Woodland Terrace then constructed "garden type" apartment buildings on the land it had acquired from the holders of its common stock. It operated and managed the project until a receiver was appointed in these proceedings.

The mortgagor defaulted in the payment of the instalment on the loan due April 1, 1957 and of all subsequently accruing instalments. On May 28, 1957 it wrote to the district office of FHA saying it was unable to meet the April instalment. It explained its financial difficulty by reference to a current vacancy rate of twenty per cent which it attributed to an excess, in past years, of new housing starts over the increase of new families in the area. It expressed the hope that its occupancy rate would improve with continued curtailment in the construction of new houses and continued growth in population. It requested a "work-out arrangement."

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[1] 12 USCA § 1743.

The State Director of FHA responded on June 13, 1957. He reported that he was informed by the Washington Office of FHA that no consideration could be given the request of Woodland Terrace for a work-out arrangement until the mortgagee elected to assign the mortgage or to acquire the property for tender to FHA. He wrote again on June 27, 1957, however, to inform Woodland Terrace that FHA officials had decided to proceed to foreclosure as soon as the mortgage was assigned.[2]

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[2] This correspondence convinces the mortgagor there was no consideration of its request for a work-out arrangement. The request, however, was not without a background. FHA was informed of the financial affairs of Woodland Terrace. The parties were involved in a current controversy over them. FHA was seeking to have restored to Woodland Terrace:

(1) The profit made by a "related" construction company on the construction of the buildings and improvements,

(2) cash disbursed by Woodland Terrace in payment for a majority of its common stock which it had purchased pro rata from its common stockholders. (This transaction occurred before enactment of the special provisions relating to "collapsible corporations." See Burge v. Commissioner, 4 Cir., 253 F.2d 765; Spangler v. Commissioner, 4 Cir., 278 F.2d 665; Bryan v. Commissioner, 4 Cir., 281 F.2d 238; Pomponio v. Commissioner, 4 Cir., 288 F.2d 827. Apparently, these disbursements were not included in the taxable income of the stockholder-recipients), and

(3) cash disbursed as ordinary, but substantial, dividends on the common stock (e.g. $400 per share, though apparently on the reduced number of shares outstanding after the earlier stock redemption).

The stockholders, denying they were obligated to restore anything to Woodland Terrace, had made an offer to pay $125,000 into the corporation on specified conditions. FHA had not accepted this conditional offer.

The merits of this earlier controversy are not before us. Its existence shows, however, that FHA, rightly or wrongly, was dissatisfied with the earlier conduct of the financial affairs of Woodland Terrace and was familiar with it.

The mortgage was assigned to FHA on July 12, 1957. Thereafter, these proceedings to foreclose the mortgage were commenced.

The mortgagor concedes it would have no defense to foreclosure by the mortgagee. The mortgage expressly contemplates foreclosure in the event of default and a deficiency judgment if the mortgaged property brings less than enough to satisfy the debt and costs. It relies upon representations which it construes as a promise by FHA not to exercise its right of foreclosure.

The United States actively promoted the construction of such projects by private business and the use of FHA insured financing. In doing so it promised to be a lenient and understanding creditor, but we agree with the District Court that it did nothing to relinquish its right of foreclosure of a mortgage in default assigned to it if it decided to pursue that course.

In passing the Veterans' Emergency Housing Act of 1946,[3] the Congress found that the combination of the return of veterans of World War II and a long-term housing shortage had created an unprecedented emergency. It called upon executive agencies to exercise their emergency and other powers toward the alleviation of the housing problem.

On December 23, 1946, President Truman announced that a vigorous housing program would be continued into 1947. He emphasized particularly the need of rental housing for returning veterans.

On January 2, 1947, the Commissioner of the Federal Housing Administration wrote to the directors of all FHA field offices, outlining a program for the construction of rental housing for veterans. Among other things, he outlined steps which had been taken to simplify procedures

[3] 60 Stat. 207, § 1(a).

in the approval and financing of § 608 projects. He said action was being taken to expedite the handling of requests for prevailing wage determinations by the Department of Labor.[4] With respect to the adjustment of the terms of mortgages, he said:

> "Adjustment of Section 608 Mortgage Terms
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> "So that housing projects constructed under the present emergency conditions may continue to maintain their competitive market position after the housing shortage is met, the Federal Housing Administration will, in collaboration with lending institutions, give consideration to a readjustment of project mortgage terms where it is deemed necessary."

Statements of similar import appeared in press releases and other documents. With the one exception noted below, they all clearly stated that in appropriate cases consideration would be given to the adjustment of mortgage terms, and committed the United States to no specific adjustment of the terms of any mortgage.

On January 7, 1947, the Assistant Commissioner sent to the directors of the field offices a circular which the directors disseminated to builders, realtors and others. This circular referred to President Truman's statement, the Commissioner's letter of January 2, 1947, and it listed a number of steps which had been taken to simplify procedures under § 608. In this list, there was the following paragraph:

> "e. Action has been taken to expedite the handling of requests for prevailing wage determinations by the Department of Labor and provisions made for the adjustment of mortgage terms, where it is deemed necessary in order that rental projects, constructed under the present emergency, may continue to maintain their competitive market position."

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[4] Wages of construction workers on such projects were required to be not less than the prevailing wages in the area as determined

This statement was clearly referable to procedures. The record discloses internal provisions for handling requests for the adjustment of mortgage terms in appropriate cases. Announcement of the establishment of such procedures cannot be construed as a general representation that, whenever earnings were adversely affected by low occupancy rates, mortgage terms would be so adjusted as to obviate all defaults. We agree with the District Court that these representations gave assurance of consideration of requests for modification of the terms of mortgages in appropriate cases, but cannot be construed as a relinquishment of the right of foreclosure.

There was also testimony that on January 15, 1947 at an area meeting sponsored by FHA for the information of people interested in considering construction of § 608 projects, representatives of FHA stated that, in the event of a default, FHA would exercise its right as preferred stockholder to take active charge of the management of the corporation and would operate the project, for the benefit of the common stockholders, until the default was remedied. Some of those who, over two years later, became the promoters and stockholders of Woodland Terrace testified they heard and relied upon such statements.

If these statements were made,[5] they do not aid the mortgagor here.

FHA's position as preferred stockholder and the charter provisions giving it the right, in specified circumstances, to replace the Board of Directors and assume active management of the company, were among the many things required by FHA as prerequisites to its insurance of the mortgage. These requirements were imposed for the protection of FHA, not for the benefit of the holders of the common stock of the mortgagor. Doubtless, if FHA exercised the right to assume immediate control of the affairs

[5] The findings below do not resolve the factual question.

of the mortgagor, it would have a fiduciary duty of conservation and avoidance of waste of the stockholders' equity, if there was one. The naked, unexercised power, however, is not inconsistent with the right of foreclosure. Whether FHA could have pursued both remedies at once, it clearly could elect to pursue either.

If, in these circumstances, representatives of FHA made the statements attributed to them, that the right of foreclosure would not be exercised and the right of management would be exercised solely for the possible advantage of the common stockholders and not for the minimization of FHA losses, their statements were in conflict with the purpose and intent of the statute and the regulations. Such unauthorized statements cannot bind the United States or work an estoppel against its exercise of a right clearly defined in the statute and reserved in the mortgage.[6]

These statements and the written representations relating to modification of mortgage terms were made early in 1947. Woodland Terrace was organized on April 12, 1949 and its note and mortgage were dated May 5, 1949. In the intervening two years, nothing resembling the mortgagor's interpretation of the written representations or the oral statements had become embodied in the statute, in FHA's detailed regulations or in its approved mortgage or charter forms. Because of this, the District Court and the Master advanced the alternative ground that resort to the written representations and the oral statements to modify the terms of the integrated agreement were barred by the parol evidence rule. There may be justification for the alternative ground, for FHA, though not a formal party to the mortgage, was the controlling party in fact and through its commitment and insuring agreement it was a formal party to the transaction.

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[6] United States v. Anderson Apartments, Inc., D.C., W.D.S.C., 114 F.Supp. 69.

We need not consider the parol evidence rule, for we think the primary ground is sufficient, that the written representations, properly interpreted, are not inconsistent with foreclosure here and that the oral statements, if made at all, are not binding. These views, however, are buttressed by the fact that in 1949 Woodland Terrace accepted the prescribed charter provisions, subscribed unreservedly to the mortgage and subjected itself unconditionally to the governing regulations of FHA. If its sponsors then thought what they now assert, it would be expected that they would have spoken then of their claim of an inconsistent agreement.

Next, the mortgagor seeks to bring itself within the rule that agency action in violation of its own procedural regulations is invalid. It says the record does not show that local representatives of FHA extended aid or advice to it or made any recommendation as to modification of mortgage terms as required or authorized by its operating manuals. The mortgagor, however, undertook to show no departure from controlling procedural regulations. It contends only that the record does not contain affirmative evidence of procedural regularity.

FHA was not required to offer such evidence. It would be wholly useless to require it in every foreclosure proceeding to affirmatively prove procedural regularity at all levels with respect to every step, when no evidence of irregularity had been offered. The burden of going forward was upon the mortgagor.[7]

Finally, the mortgagor contends that FHA is not entitled to a deficiency judgment. The mortgage provides for such a judgment, if, on foreclosure, the proceeds of sale of the mortgaged property are insufficient to satisfy the debt.

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[7] See United States *ex rel.* Accardi v. Shaughnessy, 347 U.S. 260, 74 S.Ct. 499, 98 L.Ed. 681; Shaughnessy v. United States *ex rel.* Accardi, 349 U.S. 280, 75 S. Ct. 746, 99 L.Ed. 1074; Service v. Dulles, 354 U.S. 363, 77 S.Ct. 1152, 1 L.Ed. 2d 1403.

Woodland Terrace says, however, that FHA was prohibited from being a mortgagee, being limited to insuring against loss financial institutions which were approved mortgagees. This leads it to the conclusion that FHA, as assignee of an approved mortgagee, may pursue only those remedies provided by the mortgage or by local law which were specifically authorized by Congress.

The conclusion is not required by the premise. The restriction was for the purpose of conserving the funds of FHA. It was to make certain that FHA did not undertake the direct financing of new housing but limited itself to the protection against loss of financial institutions which, with FHA approval, did finance such construction. There is nothing in the restriction or its purpose to suggest that FHA, as assignee, may not exercise remedial rights which the mortgagor expressly conferred upon the mortgagee and its assignees.

It is true that, when Congress enacted § 608[8] it incorporated by reference the provisions of § 207(k)[9] which gives FHA the right to foreclose mortgages which it has acquired by assignment and, pending acquisition of title to the mortgaged property, to exercise all of the rights of a mortgagee. It did not incorporate by reference the provisions of § 207 (l),[10] which, among other things, authorizes FHA "to pursue to final collection by way of compromise or otherwise all claims assigned" to it in connection with transfers to it of insured mortgages or mortgaged property.

However, § 608, itself, specifically contemplates the assignment to FHA "of all claims of the mortgagee against the mortgagor or others arising out of the mortgage

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[8] 12 USCA § 1743(f).

[9] 12 USCA § 1713(k).

[10] 12 USCA § 1713(l).

transaction."[11] If Congress had intended to prohibit FHA enforcement of such claims, it would have been purposeless to authorize their acquisition and to condition the mortgagee's right to the benefit of the insurance upon their assignment. Indeed, prosecution of such claims as an incident of foreclosure would seem to be the exercise of one of the rights of the mortgagee authorized by § 207(k), incorporated by reference in § 608. When, in a foreclosure proceeding, FHA seeks a deficiency judgment, it exercises that right of the mortgagee before, and, therefore, "pending," its acquisition of title to the mortgaged property within the meaning of § 207(k).

We find no error in the judgment of the District Court.

Affirmed.

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[11] 12 USCA § 1743(e).

APPENDIX B

JUDGMENT BELOW

Decree

Filed and Entered August 5, 1961

UNITED STATES COURT OF APPEALS
FOR THE FOURTH CIRCUIT

No. 8244

UNITED STATES OF AMERICA, *Appellee*,

vs.

WOODLAND TERRACE, INC., *Appellant*.

APPEAL FROM the United States District Court for the Eastern District of South Carolina.

THIS CAUSE came on to be heard on the record from the United States District Court for the Eastern District of South Carolina, and was argued by counsel.

ON CONSIDERATION WHEREOF, It is now here ordered, adjudged and decreed by this Court that the decree of the said District Court appealed from, in this cause, be, and the same is hereby, affirmed.

MORRIS A. SOPER
United States Circuit Judge.

CLEMENT F. HAYNSWORTH, JR.
United States Circuit Judge.

HERBERT S. BOREMAN
United States Circuit Judge.

APPENDIX C

Additional FHA Regulations Involved

1. 24 CFR (1959 ed.) § 232.25, first adopted under its present heading in 1954, see note 5, p. 14, *supra*, and applicable according to the notation at the head of Part 232 of Title 24, CFR, to § 207 of the National Housing Act, as amended (12 U.S.C. § 1713), provides as follows:

> "§ 232.25 *Form of contract.* The form of contract between the mortgagor and builder shall be determined in accordance with the following:
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> "(a) If it is established to the satisfaction of the Commissioner that neither the mortgagor nor any of the officers, directors, or stockholders of the mortgagor have any interest in the builder or contractor, there may be used a lump sum form of contract providing for payment of a specified amount.
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> "(b) If it is determined by the Commissioner that the mortgagor, its officers, directors or stockholders have any interest, financial or otherwise, in the builder or contractor, the form of contract shall provide for payment of the actual cost of construction, not to exceed an upset price and may provide for payment of a builder's fixed fee in addition thereto. The builder's fixed fee shall not exceed a reasonable allowance therefor as established by the Commissioner, in accordance with customary practices in the area.
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> "(c) If it is determined by the Commissioner that the mortgagor, its officers, directors or stockholders have any interest, financial or otherwise, in any subcontractor or material supplier, the mortgagor must certify in a form prescribed by the Commissioner prior to final endorsement of the mortgage for insurance that the amounts paid to such subcontractor or material supplier were not more than the rate prevailing in the locality for similar type labor and materials."

2. The following sections of Part 280 of Title 24, CFR (1949 ed.), according to its heading, interpret or apply

§ 608 of the National Housing Act, as amended (12 U.S.C. § 1743; R. 222-226):

"§ 280.10 *Mortgage must be on approved form.* To be eligible for insurance, the mortgage must be executed upon a form approved by the Commissioner for use in the jurisdiction in which the property covered by the mortgage is situated by a mortgagor with the qualifications set forth in §§ 280.23, 280.24, 280.25, 280.26, must be a first lien upon property that conforms with the property standards prescribed by the Commissioner, and the mortgagee must be obligated, as a part of the mortgage transaction, to disburse the entire principal amount of the mortgage to, or for the account of, the mortgagor.

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"§ 280.18 *Rights and remedies of mortgagee in event of default or foreclosure.* The mortgage must contain a provision or provisions satisfactory to the Commissioner, giving to the mortgagee, in the event of default or foreclosure of the mortgage, such rights and remedies for the protection and preservation of the property covered by the mortgage and the income therefrom, as are available under the law or custom of the jurisdiction."

3. The following sections of Part 282 of Title 24, CFR (1949 ed.), according to its heading, interpret or apply § 608 of the National Housing Act, as amended (12 U.S.C. § 1743; R. 222-226):

"§ 282.10 *Computation of benefits received by conveyance.* If the mortgagee elects to proceed under, and does proceed under and in accordance with, the provisions of § 282.8 (b) and at any time within thirty (30) days (or such further time as may be allowed by the Commissioner in writing) after acquiring title to and possession of the mortgaged property in accordance with such section, tenders to the Commissioner possession thereof and a deed thereto containing a covenant which warrants against acts of the mortgagee and of all parties claiming by, through, or under the mortgagee, conveying title to such property satisfac-

tory to the Commission, as provided in § 282.11, and assigns (without recourse or warranty) any and all claims which it has acquired in connection with the mortgage transaction and as a result of the foreclosure proceedings or other means by which it acquired such property, including but not limited to any claims on account of title insurance and fire or other hazard insurance, except such claims as may have been released with the prior approval of the Commissioner, the Commissioner shall promptly accept conveyance to such property and such assignments, notwithstanding that the buildings or improvements thereon shall be incomplete or may have been destroyed, damaged, or injured in whole or in part, and shall deliver to the mortgagee debentures and Certificate of Claim as provided in § 282.9, except that the one percent (1%) deduction set out in paragraph (a) (3) (i) thereof with respect to the amount of debentures shall not apply.

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"§ 282.12 *Evidence of title.* The mortgagee, at the time a deed is tendered in accordance with § 282.10, shall furnish to the Commissioner without expense to him satisfactory evidence of such title. Such title evidence shall be executed as of a date to include the recordation of the deed to the Commissioner and, shall be in the form of an owner's policy of title insurance, or a satisfactory abstract and attorney's opinion covering the period subsequent to the recording of the mortgage, or a satisfactory continuation of the title evidence accepted by the Commissioner at the time the mortgage was insured, depending upon the form of title evidence originally accepted by the Commissioner.

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§ 282.14 *Mortgage default or prepayment.* If after the mortgage becomes in default, as provided in § 282.8, the mortgagee does not make the assignment provided in § 282.8 (a), or does not foreclose or otherwise acquire the mortgaged property and make the conveyance provided in § 282.10, and written notice thereof is given to the Commissioner; or in the event that the mortgagor pays the obligation under the mortgage in full prior to the maturity thereof and the mortgagee pays

the adjusted premium charge required under the provisions of § 282.4 of the regulations in this part and written notice thereof is given to the Commissioner, the obligation to pay the annual premium charge shall cease, and all rights of the mortgagee and the mortgagor under §§ 282.9 and 282.10 shall terminate as of the date of such notice."